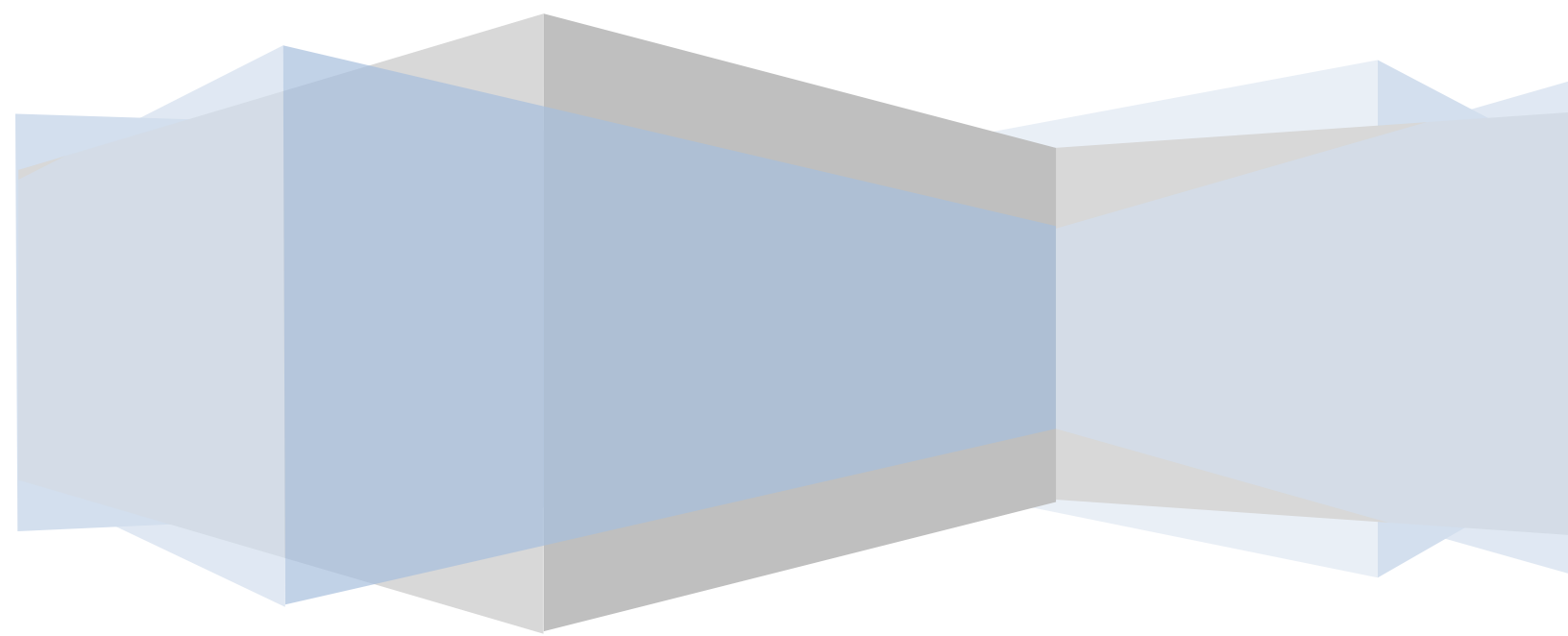

GEORGIA PERFORMANCE STANDARDS

Unit 2: “The Choice is Yours”



**Georgia Council on
Economic Education**



GEORGIA PERFORMANCE STANDARDS

SSEF1 The student will explain why limited productive resources and unlimited wants result in scarcity, opportunity costs and trade offs for individuals, businesses and governments.

Individuals have wants that are, for practical purposes, unlimited. But the total resources of society, including natural resources, human resources, capital goods and entrepreneurship, are limited, so that scarcity exists. As a result, it isn't possible for everyone to have everything he or she wants. No society has ever had enough resources to produce the full amount and variety of goods and services its members wanted. In a world of scarcity, producing any one good or service means that other goods and services cannot be produced, and trade-offs are inevitable.

a. define scarcity as a basic condition which exists when unlimited wants exceed limited productive resources

Scarcity is the condition that exists because human wants exceed the capacity of available resources to satisfy those wants; also a situation in which a resource has more than one valuable use. The problem of scarcity faces all individuals and organizations, including firms and government agencies.

b. define and give examples of productive resources as land (natural), labor (human), capital (capital goods), entrepreneurship

Productive resources are used to produce goods and services. Productive resources are classified into four categories. Land stands for natural resources or gifts of nature such as oil, iron ore, forests and water. Labor refers to human resources. Labor is more than the number of people willing and able to work. Labor also reflects the abilities of people and includes people's health, strength, education, motivation and skills. Capital refers to goods and services such as buildings, equipment, roads, dams and machinery. The level of technology also influences capital. Finally, entrepreneurship is a special kind of labor that represents the characteristics of people who assume the risk of organizing land, labor and capital resources to produce goods and services.

c. list a variety of strategies for allocating scarce resources

For a list of allocation strategies, see the table on back page of this document.

d. define opportunity cost as the next best alternative given up when individuals, businesses and governments confront scarcity by making choices.

Opportunity cost is what you must give up to obtain something else, the second-best alternative. However, what you must give up to obtain, say, a bicycle is not really money--it is whatever other good or service you would have spent the money on as your next-favorite choice. Similarly, what a government gives up to obtain, say, more educational services is not really money either--it is whatever alternative goods or services the government could have purchased instead, or the goods and services that individuals might have purchased if their taxes had been lower.

Opportunity cost includes all costs, including those of time or alternative activities. For example, one part of the opportunity cost of attending college is the money that could have been spent on something else, but another part is the cost in terms of time or alternative activities, when a student could have been working and earning income. As a different example, the opportunity cost for a business of holding a three-hour meeting with 30 employees attending isn't an additional monetary cost, since they are paying the employees already; instead, the opportunity cost of the meeting is the work that could have been accomplished if people hadn't had to attend the meeting. The opportunity cost of the meeting is the next-best alternative use of the time spent at the meeting.

A trade-off is the giving up of one benefit or advantage in order to gain another regarded as more favorable.

SSEF2 The student will give examples of how rational decision making entails comparing the marginal benefits and the marginal costs of an action.

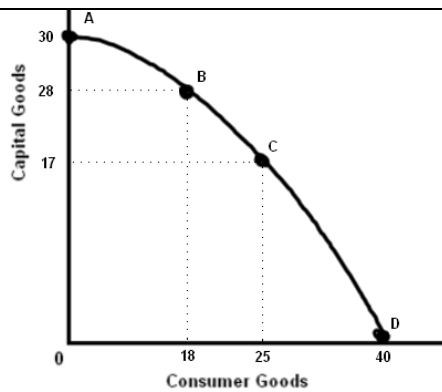
Decision making refers to the process by which rational consumers seeking their own happiness or utility will make choices. The process begins by defining the range of options that are possible. The next steps are to evaluate the costs, benefits and trade-offs involved in each choice and to reach a decision. Since people have different preferences and face different life situations, there is no expectation that all people will make the same ultimate decision. Not even economists believe that people always follow this decision-making process carefully since decision making is costly. But economists do believe that, at least implicitly, people do consider their options and trade-offs and try to make the choice that brings them the greatest satisfaction.

Cost-benefit analysis is a technique for deciding whether an action should be taken by comparing its benefits and costs. It can be applied by individuals, firms or governments. However, difficulties often arise when cost-benefit analysis is used by government; for example, it can be difficult for a government agency to compare anticipated costs and benefits. If a cost of \$100 million means that the view over the Grand Canyon is improved by 20 percent, how can an unbiased analyst decide if the benefit exceeds the cost? Thus, cost-benefit analysis often ends up using somewhat controversial assumptions to put monetary values on lives saved, days of sickness avoided, wildlife habitat protected and so on. Nevertheless, cost-benefit analysis provides a useful way of summarizing a great deal of information and organizing decision making.

a. illustrate by means of a production possibilities curve the trade offs between two options

Production Possibilities Curve

A table or graph that shows the full employment capacity of an economy in the form of possible combinations of two goods, or two bundles of goods, that could be produced with a given amount of productive resources and level of technology.



In the graph above, a movement from Point B to Point C indicates that this society now prefers to build more consumer goods and less capital goods. This movement from Point B to Point C shows the tradeoff involved in choosing a different combination of goods. In order to gain more consumer goods this society is unable to consume as many capital goods.

b. explain that rational decisions occur when the marginal benefits of an action equal or exceed the marginal costs.

Economic decisions are always made on the basis of marginal costs and marginal benefits. For example, the marginal cost of producing a good is the additional cost of producing one more unit of the good. Similarly, the marginal benefit of consuming a good is the additional value of consuming one more unit of it. Marginalism is critically important in understanding decision making because almost all of the decisions we make are marginal, as opposed to all-or-none decisions. For example, we don't make decisions between spending the entire day watching TV or the entire day studying. Instead, we choose between spending a little more time studying and a little less time watching TV, or vice versa. So a decision between studying and watching TV involves comparing the marginal benefit of studying with the marginal benefit of watching TV, not comparing their total benefit. The total benefit of studying could be far greater than the total benefit of watching TV, but after several hours of studying, the marginal benefit of studying could be less than the marginal benefit of watching TV.

SSEF6 The student will explain how productivity, economic growth and future standards of living are influenced by investment in factories, machinery, new technology and the health, education and training of people.

a. define productivity as the relationship of inputs to outputs

Productivity is measured as the quantity of output per unit of input. For example, labor productivity is measured as the quantity of output produced by an economy divided by the number of hours of labor input. A more complex measure of productivity is the quantity of output produced by all inputs. An increase in productivity means producing more goods and services with the same amount of resources, producing the same amount of goods and services with fewer resources or a combination of the two possibilities. Over time, productivity growth means that the average worker is producing more per hour, which means that the average standard of living in the economy will be higher. This assumes that the additional output is of goods and services that people value. Producing more output that is of no value is not a real increase in productivity.

b. give illustrations of investment in equipment and technology and explain their relationship to economic growth

Economic growth refers to the ability of the economy to increase its total real output or real GDP, or its real output per person. Economic growth comes from several sources: improvements in the education, experience and skill level of the workforce, sometimes called human capital; greater amounts of physical capital, that is, plant and equipment per worker; and improved technology. Economic growth is critical to job-creation and economic well-being. Economic growth slows down as the economy approaches its peak and becomes negative as it goes into recession. Economic growth begins increasing back toward zero as the economy approaches its trough and becomes positive as it begins its recovery.

c. give examples of how investment in education can lead to a higher standard of living

Economic development is a sustained increase in the standard of living of a country's population. Broadly understood, the standard of living includes a rise in the average incomes of the population as measured by real per capita GDP, and also improvements in health and education, some social protection from poverty, freedom, a rule of law and other social goals. Standard of living is defined as the level of subsistence of a nation, social class or individual with reference to the adequacy of necessities and comforts of daily life. Although economic development does focus on the material standard of living, it is a broader term than just economic growth. Economic development is facilitated by high investment levels in physical and human capital, higher productivity, competitive markets, low inflation, political stability and free trade. Incentives that increase factors contributing to economic development are greater economic freedom, protection of property rights and sound monetary policies.

SSEPF1 The student will apply rational decision making to personal spending and savings choices.

Decision making refers to the process by which rational consumers seeking their own happiness or utility will make choices. The process begins by defining the range of options that are possible. The next steps are to evaluate the costs, benefits and trade-offs involved in each choice and to reach a decision. Since people have different preferences and face different life situations, there is no expectation that all people will make the same ultimate decision. Not even economists believe that people always follow this decision-making process carefully since decision making is costly. But economists do believe that, at least implicitly, people do consider their options and trade-offs and try to make the choice that brings them the greatest satisfaction.

a. explain that people respond to positive and negative incentives in predictable ways

An incentive is a cost or benefit that motivates a decision or action by consumers, workers, firms or other participants in the economy. Higher or lower prices provide incentives; specifically, higher prices give consumers an incentive to buy less and firms an incentive to produce more. Higher and lower wages provide incentives; that is, many people will work longer or harder for higher wages, but firms will try to hire a lower quantity of workers if wages are higher. Interest rates provide incentives too; people have a greater incentive to borrow money to purchase a home or a car if interest rates are lower. The primary incentive for firms is to earn a greater profit. Economists take the principle that people respond to incentives very seriously. In every decision, incentives matter.

b. use a rational decision making model to select one option over another

P – What is the PROBLEM?

- What decision are you trying to make?
- What is the issue at hand?

A – What are the ALTERNATIVES?

- What actions are you considering?
- What options are available to you in this decision?

C – What are the CRITERIA important to the decision?

- What goals do you hope to accomplish in making your decision?
- What characteristics are you looking for in your result?
- Which criteria are more important than others? How do you rank them?

E – EVALUATE each alternative.

- Evaluate each alternative on the basis of each criterion.
- Give each alternative a plus (+) or a minus (-) according to how well it meets each criterion.

D – Make a DECISION.

- Calculate the net value of each alternative; which alternative best meets your highest-ranking criteria?
- What do you gain with each alternative?
- What do you give up with each alternative?

Decision-Making Grid

A graph-like form into which people may enter notations about the costs and benefits of various alternatives; used for assistance in making decisions.

Using the decision grid below, evaluate each option and then decide which choice you would have made.

Evaluate each alternative as:

+ = Greater benefit than cost

? = Equal or questionable
benefit and cost

- = Greater cost than benefit

Criteria	Criterion A	Criterion B	Criterion C	Criterion D
Alternative	<i>Ranking ____</i>	<i>Ranking ____</i>	<i>Ranking ____</i>	<i>Ranking ____</i>
<i>Option #1</i>				
<i>Option #2</i>				
<i>Option #3</i>				

Using the decision grid, rank the candidates in order of preference

1 _____

2 _____

3 _____

c. create a savings or financial investment plan for a future goal.

Broadly speaking, an individual has only two choices about what to do with (after-tax) income: spending on current consumption or saving for the future.

From an individual point of view, saving typically becomes a form of investing, since the saving is put into a bank account, stock, bond or mutual fund that pays a rate of return. In general, investing refers to postponing current consumption or rewards to pursue an activity with expectations of greater benefits in the future. Financial investment refers to the decisions by individuals and firms to invest money in financial assets such as bank accounts, certificates of deposit, stocks, bonds and mutual funds. Financial investment is crucial to accumulating personal wealth.

Real investment or physical capital investment is the component of aggregate demand that refers to the decisions by firms to purchase equipment and physical plant, and also the purchases of new homes by consumers. The amount of real investment is critical to economic growth. Financial investment and real investment are connected, but they are not the same. Thus, when you hear a casual reference to "investment," be clear in your own mind on whether it is financial investment or real investment.

SSEPF6 The student will describe how the earnings of workers are determined in the marketplace

a. identify skills which are required to be successful in the workplace

Competent workers in the high-performance workplace need:

Basic Skills – reading, writing, arithmetic and mathematics, speaking and listening;

Thinking Skills – the ability to learn, to reason, to think creatively, to make decisions, and to solve problems;

Personal Qualities – individual responsibility, self-esteem and self-management, sociability, and integrity.

b. explain the significance of investment in education, training and skill development.

Human capital refers to the combination of a person's education, knowledge, experience, health, habits, training and talent. A person who has acquired more human capital will be able to produce more. At the individual level, additions to human capital are closely connected to earning higher wages and income. At the level of the national economy, gains in the average level of human capital for the population are a primary source of productivity growth and economic growth. Human capital does not increase because someone earns a particular degree. It increases because one learns something in the process of earning that degree. People improve their human capital by investing in themselves in thousands of ways, but most of the ways involve study, practice and self-discipline.

Sample Resource Allocation Strategies

Strategy	Description	Advantage	Disadvantage
price	resource goes to those who use market mechanisms such as trade, barter, or price	<i>great for those who have money or a job with income</i>	<i>not good for those who have little or no income</i>
majority rule	resource goes to those who win an election; voting; consensus; largest number of people are satisfied	<i>great for those who are popular and those who have many members</i>	<i>not good for the unpopular; those who don't have the skills to form alliances</i>
contests	resource goes to the most competitive – winner of a race or arm wrestle; survival of the fittest	<i>great for those who are talented and skillful</i>	<i>not good for those who aren't competitive; unskilled</i>
Force	resource goes to the one who is strongest (physical, mental, political); most forceful	<i>great for those who are strong, powerful, bullish</i>	<i>not good for those who are weak, small, easily intimidated</i>
sharing	resource goes to multiple parties by dividing the resource	<i>great in that everyone gets an equal part; no one is left out</i>	<i>not good in that some resources can't be divided; no party may get enough; not everyone wants some of every resource</i>
Lottery	resource goes to the luckiest; random; fair	<i>great for those who are lucky and win things; everyone has an equal chance; random winners</i>	<i>not good for those who are unlucky or who "never win anything"</i>
command	resource goes where directed, ordered, told by another person	<i>great for those who are liked by the commander or if the planner is always fair</i>	<i>not good if the planner isn't fair</i>
first-come, first-served	resource goes to the early bird; first in line	<i>great for those who are quick, willing to get ahead of the crowd</i>	<i>not good for the procrastinator; those who are late in planning/preparing</i>
personal characteristics	resource goes to the one with the greatest tenure, the longest hair, the oldest, the youngest, the bluest eyes, etc.	<i>great for those who are able to set the personal characteristic to be awarded the resource</i>	<i>not good for those unable to influence the selection of the characteristic category</i>